Office - Supreme Court, U.S.
FILED
SEP 3 1982
ALEXANDER L. STEVAS,
CLERK

No. 81-523

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

CONTAINER CORPORATION OF AMERICA,
Appellant,

v.

FRANCHISE TAX BOARD,
Appellee.

ON APPEAL FROM THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA
FOR THE FIRST APPELLATE DISTRICT

BRIEF OF CATERPILLAR TRACTOR CO. AS AMICUS CURIAE IN SUPPORT OF APPELLEE

DON S. HARNACK
(Counsel of Record)
JOHN E. GAGGINI
SUSAN J. BERMAN
McDERMOTT, WILL & EMERY
111 W. Monroe Street
Chicago, Illinois 60603
(312) 372-2000
Attorneys for Amicus Curiae

Of Counsel:
RICHARD A. HANSON
1500 Washington Building
Seattle, Washington 98111
(206) 292-1144

CHAS. P. YOUNG CHICAGO, INC.

QUESTION PRESENTED

Does California's use of the combined method of apportionment to determine the amount of Container's income properly apportionable to California for state income tax purposes violate the Commerce Clause?

TABLE OF CONTENTS

	PAGE
QUESTION PRESENTED	i
TABLE OF CONTENTS	ii
TABLE OF AUTHORITIES	iii
INTEREST OF CATERPILLAR TRACTOR CO.	1
SUMMARY OF ARGUMENT	2
ARGUMENT	4
I. MISAPPORTIONMENT OF INCOME	5
II. DOUBLE TAXATION	7
III. TAXATION OF FOREIGN INCOME-PRODUCING ENTITIES	9
IV. THE RULE OF NATIONS	10
V. SPEAKING WITH ONE VOICE	12
VI. TENSIONS	12
VII. NON-UNITARY BUSINESSES CANNOT BE COMBINED	14
VIII. BUSINESS SITUS DOES NOT DICTATE A STATE'S METHOD OF APPORTIONMENT	14
CONCLUSION	16

TABLE OF AUTHORITIES

Cases: PAGE

ASARCO Inc. v. *Idaho State Tax Commission*, 50 U.S.L.W. 4962 (1982) 5, 7, 9, 13, 14

Barclay & Co. v. *Edwards*, 267 U.S. 442, 69 L.Ed. 703, 45 S.Ct. 135 (1924)..... 13

Bass, Ratcliff & Gretton, Ltd. v. *State Tax Commission*, 266 U.S. 271, 69 L.Ed. 282, 45 S.Ct. 82 (1924) 6, 8, 9, 11, 14

Bob-Lo Excursion Co. v. *Michigan*, 333 U.S. 28, 92 L.Ed. 455, 68 S.Ct. 358 (1948)..... 13

Caterpillar Tractor Co. v. *Lenckos*, 84 Ill.2d 102, 417 N.E.2d 1343 (1981), *prob. juris. noted sub. nom. Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.*, (No. 81-349) (U.S. Sup. Ct.).. 2, 5, 7, 11, 13

Container Corp. of America v. *Franchise Tax Board*, 117 Cal. App.3d 988, 173 Cal. Rptr. 121, *appeal filed*, 50 U.S.L.W. 3177 (No. 81-523)..... 5, 11, 13

Dept. of Revenue of Washington v. *Association of Washington Stevedoring Companies*, 435 U.S. 734, 55 L.Ed.2d 682, 98 S.Ct. 1388 (1978)..... 14

Exxon Corp. v. *Wisconsin Dept. of Revenue*, 447 U.S. 207, 65 L.Ed.2d 66, 100 S.Ct. 2109 (1980)..... 14

F. W. Woolworth Co. v. *Taxation & Revenue Dept.*, 50 U.S.L.W. 4957 (1982) 7, 9, 13, 14

Hans Rees' Sons, Inc. v. *North Carolina*, 283 U.S. 123, 75 L.Ed. 879, 51 S.Ct. 385 (1931)..... 7, 15

Hines v. *Davidowitz*, 312 U.S. 52, 85 L.Ed. 581, 61 S.Ct. 399 (1940)..... 11

Japan Line, Ltd. v. *County of Los Angeles*, 441 U.S. 434, 60 L.Ed.2d 336, 99 S.Ct. 1813 (1979)..... 7

Maine v. *Grand Trunk Ry. Co.*, 142 U.S. 217, 35 L.Ed. 994, 12 S.Ct. 121 (1891)..... 9

PAGE

McCulloch v. *Maryland,* 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819) 11

Mobil Oil Corp. v. *Commissioner of Taxes,* 445 U.S. 425, 63 L.Ed.2d 510, 100 S.Ct. 1223 (1980) 3, 8, 11, 13

Moorman Mfg. Co. v. *Bair,* 437 U.S. 267, 57 L.Ed.2d 197, 98 S.Ct. 2340 (1978) 7

Underwood Typewriter Co. v. *Chamberlain,* 254 U.S. 113, 65 L.Ed. 165, 41 S.Ct. 45 (1920) 6

Union Brokerage Co. v. *Jensen,* 322 U.S. 202, 88 L.Ed. 1227, 64 S.Ct. 967 (1944) 15

Wallace v. *Hines,* 253 U.S. 66, 64 L.Ed. 782, 40 S.Ct. 435 (1920) 9

Western Live Stock v. *Bureau of Revenue,* 303 U.S. 250, 82 L.Ed. 823, 58 S.Ct. 546 (1938) 15

Wisconsin v. *J. C. Penney Co.,* 311 U.S. 435, 85 L.Ed. 267, 61 S.Ct. 246 (1940) 9

United States Constitution:

Commerce Clause, Article I, Section 8, Clause 3 ..... i, 1, 2, 3, 4, 5, 7, 13, 14, 15, 16

Fourteenth Amendment, Section 1 ..... 2, 4, 12, 14

Miscellaneous:

The Federalist No. 32 (J. Cooke ed. 1961) (Hamilton) 11

Third Protocol to the 1975 Income Tax Convention with the United Kingdom of Great Britain and Northern Ireland, As Amended, S. Exec. Rep. No. 96-5, 96th Cong., 1st Sess. 6 (June 15, 1979), *reprinted in* 2 Tax Treaties (CCH) ¶8103DF 10

Tax Treaties with The United Kingdom, The Republic of Korea and the Republic of the Philippines, Hearings Before the Senate Committee on Foreign Relations, 95th Cong., 1st Sess. (1977) 10

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

CONTAINER CORPORATION OF AMERICA,

Appellant,

v.

FRANCHISE TAX BOARD,

Appellee.

ON APPEAL FROM THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA
FOR THE FIRST APPELLATE DISTRICT

BRIEF OF CATERPILLAR TRACTOR CO. AS AMICUS CURIAE IN SUPPORT OF APPELLEE

INTEREST OF CATERPILLAR TRACTOR CO.

Caterpillar Tractor Co. ("Caterpillar"), with the consent of the parties, submits this Brief as Amicus Curiae in support of Appellee's position that worldwide combination does not violate the Commerce Clause. Caterpillar is the parent of a multicorporate unitary business enterprise, incorporated in California and headquartered in Illinois. Its twenty-six wholly-owned subsidiaries operate in the United States and abroad. Collectively, they constitute the largest manufacturer and marketer of earth-moving, construction and material handling equipment in the world.

Like Container Corporation of America ("Container"), Caterpillar has also been taxed by a state on the basis of a worldwide combined report. Unlike Container, however, Caterpillar believes that the combined method of reporting properly recognizes the integrated nature of a unitary business, and thus results in a tax that is both fairly apportioned and constitutionally valid.

The constitutionality of worldwide combination as applied to Caterpillar is the subject of an appeal presently pending in this Court. *Caterpillar Tractor Co.* v. *Lenckos*, 84 Ill.2d 102, 417 N.E.2d 1343 (1981), *prob. juris. noted sub. nom. Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.*, (No. 81-349). The disposition of the present case may affect the issues in question in Caterpillar's case.

SUMMARY OF ARGUMENT

Appellant contends that application of worldwide combined reporting inherently violates the Commerce Clause (U.S. Const. art. 1, § 8, cl. 3). The record in *Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.*, (No. 81-349) establishes, however, that this apportionment method is constitutional both on its face and in effect when applied to the domestic parent of a worldwide unitary business. Indeed, combined reporting in the case of *Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.* is the only method that fairly reflects the business activity of Caterpillar within Illinois.

Combined reporting is, in essence, the equivalent of formulary apportionment applied to a multicorporate unitary business. The combined method of apportionment is justified by the inability to isolate the source of profits earned by a nominally separate enterprise within the multicorporate group. It should not result in misapportionment of income when the business is truly integrated. If distortion occurs because the various facets of the business are in fact discrete, or if the business is unitary and significant misapportionment nonetheless occurs, the Due Process Clause (U.S. Const.

amend. XIV, § 1), rather than the Commerce Clause, affords relief to a taxpayer.

Combined reporting takes into account the "underlying economic realities of a unitary business." *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. 425, 441, 63 L.Ed.2d 510, 100 S.Ct. 1223 (1980). It is irrelevant that Container or Caterpillar chooses to operate as a domestic parent with foreign subsidiaries rather than as a single domestic corporation engaged directly in foreign business. It must be conceded that in this latter case, no unconstitutional double taxation results. Caterpillar submits that the corporate formalities existing in the former instance cannot render the same tax unconstitutional under a theory of double taxation.

Although combined reporting looks to out-of-state values in order to determine the amount of in-state income properly taxable, only the domestic corporation, in form and in substance, is taxed. Foreign assets and shareholders are unaffected by California's use of a combined apportionment formula.

There is no support for Appellant's and Amici's contention that worldwide combination violates the rule of nations. No treaty requires the states to tax domestic parent corporations in conformance with the federal arm's-length method. International custom is not implicated because California is not taxing a foreign entity. Our foreign trading partners have found no occasion to complain of variations from federal practice when the tax burden rests solely on a domestic parent corporation.

The worldwide combination of Container or Caterpillar does not infringe upon the government's ability to "speak with one voice." California's method of apportionment offends neither treaty nor foreign sovereign. World commerce is unfettered by California's tax on domestic parent corporations. Foreign countries, unaffected by apportionment of income of a domestic parent corporation, have not expressed concern with the tax imposed on Container or Caterpillar.

Rather, our trading partners have complained of the imposition of worldwide combination to apportion the income of foreign controlled unitary business enterprises. This question is not before the Court.

The distinction between foreign and domestic control may be irrelevant when a business is truly unitary. The issue is always one of limiting state taxation to the income earned within the state. If income is properly apportioned, constitutional rights are unimpaired. If income earned elsewhere is unfairly allocated to a state, the taxpayer may justly complain of a constitutional violation. The essence of the taxpayer's injury, however, is that its right to due process was infringed, rather than that the Commerce Clause was violated.

The framework of the Commerce Clause does not require this Court to dissect issues germane to worldwide combination of a domestically controlled unitary business enterprise. The questions dispositive of valid apportionment are within the exclusive province of the Due Process Clause. Those issues are, (1) whether the business enterprise is truly unitary and, if so, (2) whether the resulting apportionment significantly distorts the income earned within the state.

ARGUMENT

Appellant, Container, and substantially all of the supporting Amici urge this Court to rule that the apportionment of income of a domestically controlled unitary business enterprise by way of worldwide combination violates the Commerce Clause of the Constitution. Appellant and Amici catalog the alleged violations as including misapportionment of income, double taxation of income, taxation of foreign income-producing entities, violation of the rule of nations, interference with this country's ability to speak with one voice in foreign relations, and an irreconcilable conflict with the federal system which allegedly mandates the use of separate accounting by states.

Appellant's arguments are made in the context of its strenuous contentions that California improperly views Container and its foreign subsidiaries as a unitary business enterprise. If Appellant is correct, this appeal can be disposed of without reaching the constitutional objections to combination. *ASARCO Inc.* v. *Idaho State Tax Commission*, 50 U.S.L.W. 4962 (1982). However, as we understand Appellant's and Amici's contentions, their arguments are premised upon the assumption that the use of worldwide combination by a state violates the Commerce Clause even when applied to a unitary business enterprise.

Amicus, Caterpillar, respectfully submits that the constitutional issue raised by Appellant, i.e., whether combination of a domestically controlled worldwide unitary business enterprise to determine income properly apportioned to a state violates the Commerce Clause, can best be considered in the context of the record in *Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.*, (No. 81-349). The undisputed and extensive record in *Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.* establishes that Caterpillar operated worldwide with twenty-six subsidiary corporations. The Caterpillar operations were vertically and horizontally integrated and all parties agree that Caterpillar's worldwide business activities constitute a classic example of a unitary business enterprise. Illinois used worldwide combination to apportion the income of specific companies in the Caterpillar group to Illinois.

I. Misapportionment of Income.

The combination of Caterpillar's operations caused no misapportionment of income. If misapportionment of income is in fact present in *Container Corp. of America* v. *Franchise Tax Board*, (No. 81-523), it does not follow that the combination methodology is constitutionally flawed. Rather, such misapportionment is more likely attributable to the fact that there is insufficient economic interdependence to categorize the business enterprises of Container and its foreign subsidiaries as unitary.

The element critical to the justification of the use of formulary apportionment is a unitary business enterprise which ordinarily results in an inability to adequately identify earnings of a business enterprise on a separate basis. If *Underwood Typewriter Co.* v. *Chamberlain*, 254 U.S. 113, 65 L.Ed.165, 41 S.Ct. 45 (1920) had involved Connecticut and Canada rather than Connecticut and New York, this Court's adoption of the use of formulary apportionment would have had equal application and validity. This was subsequently demonstrated by this Court's decision in *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271, 69 L.Ed. 282, 45 S.Ct. 82 (1924), in which New York was not denied the right to tax the income derived from operations in New York simply because the taxpayer's method of accounting shifted all income to the United Kingdom.

In a truly unitary enterprise, the differing economic values existing in various geographic areas do not distort the apportionment. The income derived from an engine block manufactured in Peoria, Illinois, partially assembled in the United Kingdom, thereafter modified in France, incorporated in an earthmover in Belgium and finally sold to a Caterpillar customer in Saudi Arabia cannot be sourced on a geographic basis. The relative costs of labor, material, and sales (transportation) are melded into a unified economic effort. The contribution to the total profit made by the intervening economic activities are interdependent to each of the successive steps. While low wage rates of an area may impact upon the total pool of income, so too may high cost technology of another geographic area contribute inordinately to the pool of income. The method may be less than precise, but clearly combined apportionment fairly reflected the income earned in Illinois by Caterpillar and its domestic subsidiaries doing business in Illinois as a part of a worldwide unitary business enterprise.

If California has misapportioned Container's income because Appellant is not unitary with its foreign subsidiaries, Container's relief is dictated by this Court's decisions in

ASARCO Inc. v. *Idaho State Tax Commission,* 50 U.S.L.W. 4962 (1982) and *F. W. Woolworth* v. *Taxation & Revenue Dept.*, 50 U.S.L.W. 4957 (1982). If Container and its subsidiaries are engaged in a unitary business, but combination results in a demonstrable and significant misapportionment of the unitary business income to California, Container is also entitled to relief. *Hans Rees' Sons, Inc.* v. *North Carolina,* 283 U.S. 123, 75 L.Ed. 879, 51 S.Ct. 385 (1931); *Caterpillar Tractor Co.* v. *Lenckos,* 84 Ill.2d 102, 417 N.E.2d 1343 (1981). In either case, Container derives protection from its right to due process, not the Commerce Clause.

II. Double Taxation.

Appellant and supporting Amici argue that combination inevitably results in unconstitutional double taxation.[1] They contend that if Venezuela apportions and taxes income on a separate basis, California cannot also apportion and/or tax any portion of that income. The argument concludes that a state tax on any part of the income apportioned to Venezuela demonstrates an unconstitutional double tax which this Court's decision in *Japan Line, Ltd.* v. *County of Los Angeles,* 441 U.S. 434, 60 L.Ed.2d 336, 99 S.Ct. 1813 (1979) prohibits.

The argument, framed in the context of a domestic parent and a Venezuelan subsidiary conducting a unitary business, must be tested in the context of a single California corporation engaged in business in Venezuela by way of a permanent establishment. Appellant's argument that the apportionment of income to California which is also apportioned to Venezuela (without regard to the propriety of the respective apportionment methods) results in double taxation ignores the possibility that Venezuela has taxed income properly apportionable to California. *Moorman Mfg. Co.* v. *Bair,* 437 U.S. 267, 57 L.Ed.2d 197, 98 S.Ct. 2340 (1978).

[1] Appellant and Amici ignore the record in *Chicago Bridge & Iron Co.* v. *Caterpillar,* (No. 81-349) which proves beyond question that worldwide combination does not always result in double taxation of a unitary business enterprise.

Appellant looks only to the result, i.e., apportionment of the same dollar of income by two jurisdictions. Appellant and Amici must concede, however, that the result complained of as unconstitutional double taxation, i.e., apportionment of income to two jurisdictions, is precisely the result that is admittedly constitutional in the case of the single California corporation engaged in business in Venezuela. In that case, California may unquestionably apportion income to California based upon in-state and out-of-state factors under formulary apportionment. *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271 (1924); *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. 425 (1980). Venezuela will still determine the income of the unitary business enterprise apportionable to it on the basis that the California corporation is in substance conducting a separate economic and independent business in Venezuela.

The overlap of income and the California and Venezuela tax are identical in either case. Does it follow in the case of a single corporation engaged in a unitary business in two jurisdictions that the taxation of income by both jurisdictions is constitutional, while interjection of a subsidiary corporation in Venezuela as a participant in the unitary business enterprise renders the same result unconstitutional as double taxation? We think not. This Court has not yet permitted corporate formalities attendant a given unitary business enterprise to dictate state tax consequences. In *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. at 440 (1980), this Court rejected the taxpayer's argument that foreign dividends should be excluded from the apportionment base, stating:

> Superficially, intercorporate division might appear to be a more attractive basis for limiting apportionability. But the form of business organization may have nothing to do with the underlying unity or diversity of business enterprise. Had appellant chosen to operate its foreign subsidiaries as separate divisions of a legally as well as a functionally integrated enterprise, there is little doubt that the income derived from those divisions would

meet due process requirements for apportionability. Cf. *General Motors Corp.* v. *Washington*, 377 U.S. 436, 441 (1964). Transforming the same income into dividends from legally separate entities works no change in the underlying economic realities of a unitary business, and accordingly it ought not to affect the apportionability of income the parent receives. (Footnote omitted.)

III. Taxation of Foreign Income-Producing Entities.

Neither California nor Illinois has the right or authority to tax foreign values or foreign income. This Court has repeatedly stated that a clear and viable connection between the taxing state and the income taxed is a prerequisite to valid apportionment. *ASARCO Inc.* v. *Idaho State Tax Commission*, 50 U.S.L.W. 4962 (1982); *F. W. Woolworth Co.* v. *Taxation & Revenue Dept.*, 50 U.S.L.W. 4957 (1982). While no state can "reach profits earned elsewhere under the guise of legitimate taxation," (*Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. at 283), a state may look beyond its borders to "get the true value of the things within it, when they are part of an organic system of wide extent," *Wallace* v. *Hines*, 253 U.S. 66, 69, 64 L.Ed. 782, 40 S.Ct. 435 (1920). *See also, Maine* v. *Grand Trunk Ry. Co.*, 142 U.S. 217, 35 L.Ed. 994, 12 S.Ct. 121 (1891).

Appellant and supporting Amici urge that worldwide combination results in taxation of foreign values. This contention ignores the true function of combination as a method of apportionment. All parties recognize that a state may impose an income tax on a taxpayer having minimum necessary connections with the state. *Wisconsin* v. *J. C. Penney Co.*, 311 U.S. 435, 85 L.Ed. 267, 61 S.Ct. 246 (1940). California cannot impose a tax on Container's Columbian subsidiary or its Venezuelan subsidiary or any of its other foreign subsidiaries if those subsidiaries have no nexus to California. What Appellant and Amici ignore in this case, is that in using combined apportionment California is not intending to tax the income of Container's foreign subsidiaries. Combined apportionment is used only to determine that amount of

income attributable to Container's contributions to the unitary business conducted in California. Only Container is required to pay a tax. There is no impact upon the foreign subsidiary or upon its minority shareholders. There is no diminution of the subsidiary's equity or assets.

IV. The Rule of Nations.

Appellant and supporting Amici contend that worldwide combination deviates from the federal arm's-length method of determining the taxability of income, thereby violating the rule of nations. They argue that income tax treaties in effect between the United States and the other countries of the world, as well as international custom, mandate that the states use the identical method of apportioning income as does the federal government.

Appellant and Amici, however, misconstrue the explicit language and spirit of the U.S. treaties in effect with foreign nations. Not a single compact limits the manner in which a sovereign may tax its domestic companies. Rather, the treaties specifically provide that the host country retains sole discretion to choose the method by which it will tax its own residents. Thus, Appellant and Amici must concede that no treaty presently limits California's right to tax Container by way of worldwide combination.[2]

---

[2] Article 9(4) of the U.S./U.K. tax treaty as originally proposed would have prohibited California from applying combined reporting to the U.S. subsidiaries of U.K. corporate parents. It did not preclude California from using combination to determine the portion of unitary business income that a domestic parent, such as Container, earned within California. The Senate refused to ratify the treaty until the proposed limitation was removed. *See, Third Protocol to the 1975 Income Tax Convention with the United Kingdom of Great Britain and Northern Ireland, As Amended,* S. Exec. Rep. No. 96-5, 96th Cong., 1st Sess. 6 (June 15, 1979), *Reprinted in* 2 Tax Treaties (CCH) ¶8103DF. *See also, Tax Treaties with the United Kingdom, the Republic of Korea and the Republic of the Philippines, Hearings Before the Senate Committee on Foreign Relations,* 95th Cong., 1st Sess. (1977).

This Court has not accepted the argument that international custom demands uniformity between state and federal apportionment methods. Historically, states have enjoyed wide latitude in deviating from federal methods of taxation. *See*, Federalist No. 32 (J. Cooke ed. 1961) (Hamilton); *McCulloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316, 425, 4 L.Ed. 579 (1819); *Hines* v. *Davidowitz*, 312 U.S. 52, 68, 85 L.Ed. 581, 61 S.Ct. 399 (1940); *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271 (1924). As early as the decision in *Bass, Ratcliff*, this Court approved variations in state and federal practice. In *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. at 448, this Court reaffirmed that no requirement of consistency between federal and state taxation of income exists:

> Concurrent federal and state taxation of income, of course, is a well-established norm. Absent some explicit directive from Congress, we cannot infer that treatment of foreign income at the federal level mandates identical treatment by the States. The absence of any explicit directive to that effect is attested by the fact that Congress has long debated, but has not enacted, legislation designed to regulate state taxation of income.

The application of the "rule of nations" is particularly illusory where, as in *Container* and *Caterpillar*, the state is attempting to determine the income of a domestic parent corporation. No foreign country is implicated. Logically, there is no greater need for consistency between state and federal methods where the domestic parent is part of a unitary worldwide enterprise than where it is a part of a unitary domestic enterprise. In either circumstance, the imposition of the tax falls upon the income of the domestic parent. Appellant's superficially appealing contention that international practice imperatively requires that California use separate accounting has no merit when used as a shield to legitimate taxation of income fairly apportioned to and earned within that state.

V. Speaking With One Voice.

The combination of Container or Caterpillar on a worldwide basis has had, and will have, no impact upon the federal government's ability to speak with one voice. Appellant and supporting Amici do not claim that California's or Illinois' use of combination in the instant cases has violated any treaty provisions. The treaties cited by Appellant and Amici each pertain to the agreed method of taxation of a corporation foreign to the treaty countries' jurisdiction. None of the treaties limits the sovereign in the manner in which it will tax its domestic companies. The United States taxes Container on its world income without apportionment and grants Container foreign tax credits or deductions. California may only tax the income that Container earns in California. The method of apportionment that California uses to determine the amount of income Container earns in California in no way impinges upon world commerce.

The constitutional propriety of California's determination of the income it apportions or allocates to California on account of Container's activities in that state is limited solely by the application of the Due Process Clause. California's actions with respect to Container do not legitimately concern the federal government or any foreign government. The issues raised in this case are strictly between Container and California.

VI. Tensions.

It is specious to argue that combination as applied to Container by California or Caterpillar by Illinois creates tensions between the U.S. and its foreign trading partners. Our foreign trading partners have no reason or right to question the methods or results of federal or state taxation of domestic parent companies. Venezuela has no legitimate concern with a state income tax imposed upon Container. The U.K. has no legitimate concern with a state income tax imposed upon Caterpillar. Foreign nations have indicated concern when states use combination to apportion the income

of foreign controlled unitary business enterprises. But clearly the expressed concerns do not address the issues Container raises herein.

The issue of whether or not the Commerce Clause may indeed erect a barrier to preclude the use of worldwide combination to apportion the income of foreign-owned unitary business enterprises is not before the Court. *Mobil Oil, ASARCO, Woolworth, Caterpillar* and *Container* all involve domestic parent corporations.[3] This Court has stated that the Commerce Clause will not protect a domestic corporation operating in a foreign territory where the business is of greater concern to American interests. *Bob-Lo Excursion Co.* v. *Michigan*, 333 U.S. 28, 36, 92 L.Ed. 455, 68 S.Ct. 358 (1948).

Any additional constitutional protection afforded foreign businesses is based upon this Court's recognition that domestic corporations have:

> the power of the United States to protect their interests and redress their wrongs in whatever part of the world their business might take them, while the foreign corporations must look to the country of their origin for protection against injury or redress of losses occurring in countries other than the United States. *Barclay & Co.* v. *Edwards*, 267 U.S. 442, 447, 69 L.Ed. 703, 45 S.Ct. 135 (1924).

The states may be prohibited from imposing inordinate burdens on foreign enterprises if our nation deems it expedient to avoid offending their sovereigns' sensitivities. In the specific context of this case it is unnecessary for this

---

[3] *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. 425 (1980); *ASARCO Inc.* v. *Idaho State Tax Commission*, 50 U.S.L.W. 4962 (1982); *F. W. Woolworth Co.* v. *Taxation & Revenue Dept.*, 50 U.S.L.W. 4957 (1982); *Caterpillar Tractor Co.* v. *Lenckos*, 84 Ill.2d 102, 417 N.E. 2d 1343 (1981), *prob. juris. noted sub. nom. Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co.*, (No. 81-349); and *Container Corp. of America* v. *Franchise Tax Board*, 117 Cal. App. 3d 988, 173 Cal. Rptr. 121, *appeal filed*, 50 U.S.L.W. 3177 (No. 81-523).

Court to walk an analytical tightrope between domestically-owned and foreign-owned enterprises. Perhaps they are constitutionally distinct; perhaps they are not. In this case the issue of interference with foreign commerce is not present.

VII. Non-Unitary Businesses Cannot be Combined.

ASARCO and *F. W. Woolworth* teach that categorization as a unitary business enterprise requires much more than common control and incidental business relationships.[4] In *Exxon Corp.* the Court described *"a highly integrated business which benefits from an umbrella of centralized management and controlled interaction"* as being unitary. *Exxon Corp.* v. *Wisconsin Dept. of Revenue,* 447 U.S. 207, 224, 65 L.Ed.2d 66, 100 S.Ct. 2109 (1980). This Court's opinions demonstrate that no one measure fits all factual situations, and that states cannot "reach profits earned elsewhere under the guise of legitimate taxation." *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission,* 266 U.S. 271, 283 (1924). If this Court determines that Container's operations are not unitary, application of combined apportionment to its non-unitary, discrete business enterprises is prohibited in all instances by the Due Process Clause.

VIII. Business Situs Does Not Dictate a State's Method of Apportionment.

The Commerce Clause clearly permits California to look to a unitary business operation to determine the share of income apportionable to California. The tangential use of foreign income as a computational tool is not unconstitutional, since ultimately "[n]o foreign business or vessel is taxed." *Dept. of Revenue of Washington* v. *Association of Washington Stevedoring Companies,* 435 U.S. 734, 754, 55 L.Ed.2d 682, 98 S.Ct. 1388 (1978). There is nothing talismanic about the situs of unitary operations. The fact that some of Container's or Caterpillar's subsidiaries are located beyond

---

[4] *ASARCO Inc.* v. *Idaho State Tax Commission,* 50 U.S.L.W. 4962 (1982); *F. W. Woolworth Co.* v. *Taxation & Revenue Dept.,* 50 U.S.L.W. 4957 (1982).

the "water's edge" does not sound the death knell for a properly apportioned state income tax.

It is respectfully submitted that there is no constitutional reason which prevents California from applying worldwide combination to a domestically controlled unitary business enterprise if the taxpayer fails to establish that combination of its business enterprise has resulted in a meaningful distortion of income. *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123 (1931). It is not the purpose of the Commerce Clause to relieve those engaged in foreign commerce from their "just share of state tax burden even though it increases the cost of doing the business." *Western Live Stock* v. *Bureau of Revenue*, 303 U.S. 250, 254, 82 L.Ed. 823, 58 S.Ct. 546 (1938). To argue otherwise verges on the frivolous. The Commerce Clause does not shield Container from California's efforts to exact its just share of money due it in return for the use of the state's services. *See, Union Brokerage Co.* v. *Jensen*, 322 U.S. 202, 88 L.Ed. 1227, 64 S.Ct. 967 (1944).

Amicus Caterpillar respectfully submits that the threshold issue presented to the Court by this case is whether Container is, in fact, a participant in a unitary business enterprise with its foreign subsidiaries. The gravamen of Container's complaint must rest with California's definition of a unitary business enterprise and whether, if unitary, the resulting apportionment significantly distorts the income of Container. *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123 (1931).

CONCLUSION

If this Court approves the decision of the California Court of Appeal that Container's worldwide operations constitute a unitary business enterprise, Caterpillar respectfully urges the Court to affirm the lower court's decision that combination does not violate the Commerce Clause.

August, 1982

Respectfully submitted,

DON S. HARNACK
(Counsel of Record)
JOHN E. GAGGINI
SUSAN J. BERMAN
McDERMOTT, WILL & EMERY
111 W. Monroe Street
Chicago, Illinois 60603
(312) 372-2000
Attorneys for Amicus Curiae

Of Counsel:
RICHARD A. HANSON
1500 Washington Building
Seattle, Washington 98111
(206) 292-1144